USAID

U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

September 30, 1998

MEMORANDUM FOR AA/M, **Terrence J. Brown**

FROM: AIG/A, Everette B. Orr Everette B. Orr

SUBJECT: Audit of Post Transaction Review Activities Under the Commodity Import Program (Audit Report No. A-000-98-007-P)

This report shows that since 1993 when the Office of Procurement (OP) suspended the regularly scheduled post transaction reviews conducted under the Commodity Import Program (CIP), USAID has not ensured that commodity transactions met the pricing requirements of the Foreign Assistance Act (FAA). These reviews had identified an average of $2.6 million in overpayments annually, and related referrals to the OIG Office of Investigations (OIG/I) had led to more than $8 million in additional recoveries as well as numerous criminal prosecutions for fraudulent activities. The audit also disclosed a number of internal control weaknesses concerning separation of duties and documentation of transactions and events, as evidenced by OP's inability to account for the disposition of $2.3 million in previously identified overpayments. These conditions demonstrate that OP has not managed the CIP with a positive attitude toward instituting effective internal controls and enforcing the price provisions of the FAA. The report contains five recommendations (see pages 10, 11, 12 and 13).

In its September 16, 1998 response to our draft report, the Assistant Administrator for Management (AA/M) did not concur with the recommendations, stating that they are not applicable primarily because negotiations have been completed to transfer the post-transaction review function to USAID/Cairo on January 1, 1999. In addressing the audit findings the AA/M contends that OP has continued to take steps to identify over-pricing of commodities and expresses his belief that significant price controls exist under the private sector CIP because the nature of its operation makes it less vulnerable to pricing violations than its predecessor public sector program. The response details several areas where the AA/M believes information in the draft audit report is erroneous or misleading, and also states that M/OP staff have assured him that all available information was provided to the audit team, regardless of concerns in the draft report that OP had not provided the auditors with a written confirmation to that effect.

The AA/M's comments on the draft report, in our view, are not responsive to the CIP issues and related recommendations addressed in the report. The audit recommendations are dismissed as not applicable due to the planned transfer of the program to USAID/Cairo. But nowhere in the response is there an acknowledgment that for several years OP management has operated the CIP without an effective post transaction review program in place, that the program has been operated without an effective system of internal controls, and that there has been very little action by OP management to address these problems. Without acknowledging the problems within the context of operation of the program by OP, there is no assurance that the problems will be addressed when the program is transferred to USAID/Cairo. We believe the comments further support the conclusion we reached in our draft report that OP management has not established a supportive attitude toward internal controls and the price provisions of the FAA. Because the comments indicate a continuing lack of a supportive management attitude, we added a recommendation.

After reviewing management's comments concerning erroneous and misleading information in the draft report, reexamining our audit documentation in these areas, and discussing these areas with OP personnel, we remain convinced that the draft report presented to management represents a fair and objective assessment of OP's post transaction review activities under the CIP. Although recent correspondence between the AA/M and the USAID/Cairo Mission Director indicates that some CIP functions, including post transaction review, will be transferred to USAID/Cairo, no agreement has yet been reached detailing the specific CIP authorities, responsibilities, and functions to be transferred. Therefore, we do not agree that the AA/M's comments concerning the inapplicability of report recommendations due to the transfer of the post transaction review function represents a management decision to implement the recommendations. Based on our review of the response we have made some minor changes to the draft report and have also reworded the report recommendations to provide management more flexibility to choose a course of action to solve the identified problems. We have attached, as Appendix II, the complete management comments on the report, along with our analysis of their comments, as appropriate.

Background

USAID provides about $225 million a year in development assistance through its CIP. The CIP, which began in 1949, was designed to provide developing countries with balance of payment support. USAID makes dollars available to host governments for financing the exchange costs of procuring and shipping commodities utilized by business and industry. Private companies in the host country pay for imported commodities by depositing an equivalent amount of local currency at a participating host country bank. USAID has provided CIP funding to more than 20 countries since the program's inception. The largest CIP that USAID currently operates is a private sector program in Egypt, which began in 1986. In 1997, the CIP provided about $188 million in commodities to Egypt, which represented about 25 percent of the United States' economic assistance to Egypt and the bulk of the CIP program worldwide.

OP has been responsible for administering the program since the mid-1980's. In particular, International Trade Specialists (ITS) were assigned to OP's Monitoring Branch to oversee the program. ITS' duties included 1) recommending the approval of commodity transactions, 2) responding to supplier inquiries, 3) conducting post transaction reviews (sometimes called post audits) to ensure that commodities were not overpriced, and 4) negotiating financial settlements for any overpayments. A description of ITS duties and a diagram of the commodity transaction process is provided in Appendix III.

Audit Objective

OIG received an allegation that the Monitoring Branch suspended post transaction reviews of CIP transactions in 1993. According to the allegation, these reviews are required by regulation, had been a cost-effective use of USAID resources, and had led to the recovery of millions of dollars in overpayments. As a result of this allegation, we designed this audit to answer the following objective:

- **Does USAID conduct post transaction reviews of Commodity Import Program transactions in accordance with applicable laws and regulations?**

However, OP management would not provide us with written assurance that all relevant information has been provided. The lack of assurance that all information was provided means that deficiencies could be more severe than presented in this report.

A full description of the audit scope and methodology, including a discussion of the above disclaimer, is contained in Appendix I.

Summary of Results

Although required by federal regulations, USAID has not conducted post transaction reviews on a regular basis since some time in 1993. As a result, for over four years, OP has not ensured that commodity prices did not exceed the price prevailing in the U.S., as required by the Foreign Assistance Act (FAA) and federal regulations. Prior to 1993, post transaction reviews identified millions of dollars in overpayments each year (an average $2.6 million) and resulted in monetary recoveries that far exceeded the costs to conduct the reviews. In addition, referrals to the OIG Office of Investigations (OIG/I) led to about $8.1 million in additional recoveries as well as numerous criminal prosecutions for fraudulent activities. Since OP management stopped conducting post transaction reviews, identification and recovery of overpayments declined significantly, and referrals to OIG/I stopped completely.

Further, weak internal controls regarding separation of duties, documentation, and recording of transactions and events increase the risk of losses due to possible fraud, waste, and abuse.

In fact, USAID has been unable to account for the disposition of $2.3 million in overpayments that were identified from prior post transaction review activities.

The fact that OP has not conducted post transaction reviews on a regular basis for over four years and has not implemented an effective system of internal controls indicates that OP management has not shown a supportive attitude toward enforcing the price provisions contained in the Foreign Assistance Act and in Federal Regulations. As a result, OP has not fulfilled its responsibility to prevent overpricing and to identify and recover overpayments. Further, although OP management has proposed replacing post transaction reviews with preshipment reviews, it has not adequately supported the rationale for this approach and, after three years has not implemented the preshipment reviews.

USAID Has Not Conducted Post Transaction Reviews <u>as Required bv Regulation</u>

Some time in 1993, the Monitoring Branch stopped conducting post transaction reviews on a regular basis. Prior to 1993, overpayments identified from those reviews averaged about $2.6 million per year. After OP stopped conducting the reviews on a regular basis, identified overpayments dropped to about $302,000 per year. Our analysis shows that the branch's post transaction review activities had been cost effective by identifying about $33 and recovering about $10 in overpayments for every dollar spent conducting the reviews. Also, post transaction reviews had served as a deterrent to overpricing by commodity suppliers. The existence of the post transaction review function led some suppliers to make voluntary refunds of overpayments" These voluntary refunds have also declined. Finally, post transaction review activities identified potential fraudulent activities, many of which OIG/I presented for successful prosecution. These referrals also stopped when the reviews were suspended.

The FAA, Section 604(b) requires USAID to ensure that the price of the commodities financed under the CIP be no higher than the market price prevailing in the U.S. as adjusted for differences in the cost of transportation, quality, and terms of payment. To ensure that final actual costs of a CIP transaction do not exceed the market price, Federal Regulations (22 CFR 20 1.60, Subpart G, Price Provisions) require the Monitoring Branch to conduct post transaction reviews of commodity transactions. To perform these reviews, ITS checked transaction documentation after a transaction had been completed and the commodity had been shipped. The House Committee on Foreign Affairs, in a 1968 report on the FAA, stated that post transaction reviews (called post audits in the report) should be made in order to ensure compliance with regulations concerning price and quality.'

[1] "Foreign Assistance Act of 1968, Report of the Committee on Foreign Affairs Together With Minority, Additional, and Supplemental Views on H. R. 15263," June 26, 1968.

During a post transaction review, the ITS reviewed the cost of all major line items for a commodity transaction to determine if the transaction met USAID criteria. These line items included **the costs** for the commodity, freight, insurance, and commissions. If the ITS questioned a line item, the specialist requested additional information and documentation from the supplier. If the additional information did not satisfactorily resolve the cost discrepancy, the ITS either prepared a Bill For Collection or negotiated a voluntary refund to recover the overpayment. A Bill For Collection is a written notification that the supplier owes USAID money and is also a request for payment. By contrast, a voluntary refund is a negotiated settlement of an overpayment wherein the ITS and supplier agreed that the supplier will repay USAID for an overpayment.

OP management officials told us that they temporarily suspended the post transaction review program sometime in 1993. The officials also stated that, in 1996, OP decided to terminate the reviews permanently. However, in our review of the records of all transactions from 1991 to 1995, we found that some ITS conducted a few post transaction reviews after the suspension was in effect. Table I shows that the number of post transaction reviews dropped from 279 in 1993, to 73 in 1994, and to only 4 in 1995.

Table I

CIP POST TRANSACTION REVIEWS BY YEAR

	Number of Post Transactions Reviews	Dollar Value of Transactions Reviewed *(in Millions)*
1991	619	$123
1992	490	$ 80
1993	279	$ 55
1994	73	$21
1995	4	$ .4
1996	13	$ 5
1997	0	$ 0

Recoveries of Overpayments
Dropped Substantially

When OP suspended conducting post transaction reviews, identification and recovery of overpayments dropped substantially. Table II shows that overpayments identified in voluntary refunds and bills for collection dropped precipitously in 1993. Average annual recoveries dropped about 61 per cent, from $808,000 per year prior to the suspension of post transaction reviews (over the three years from 1990 to 1992) to $299,000 per year after the suspension (over the five years from 1993 to 1997).

Table II

OVERPAYMENTS IDENTIFIED AND **RECOVERED**[2]

	Overpayments Identified			Overpayments Recovered by OP		
	Voluntary Refunds	**Bills For Collection**	**Total**	**Voluntary Refunds**	**Bills For Collection**	**Total**
1990	**$ 201,199**	**$1,090,047**	**$1,291,246**	**$ 144,954**	**$801,370**	**$ 946,324**
1991	**$ 157,823**	**$1,911,137**	**$2,068,960**	**$ 154,562**	**$189,193**	**$343,755**[3]
1992	$ 278,811	**$4,062,036**	**$4,340,847**	$ 278,811	$854,992[4]	**$1,133,803**[5]
1993	$ 58,783	-	$ 58,783	$ 58,783	-	$ 58,783
1994	$ 55,409	-	$ 55,409	$ 55,409	-	$ 55,409
1995	$ 109,781	-	$ 109,781	$ 109,781	-	$ 109,781
1996	**$ 1,198,944**	-	**$1,198,944**	**$1,183,133**	-	**$1,183,133**[6]
1997	$ 87,886	-	$ 87,886	$ 87,886	-	$87,886
Totals	**$2,148,636**	**$7,063,220**	$ **9,211,856**	**$2,073,319**	**$1,845,555**	**$3,918,874**

[2] Because OP records were incomplete, we consolidated information from the Monitoring Branch, **Office** of Financial Management, **USAID/Cairo,** and OIG investigative files to present the best possible listing of overpayments identified and recovered by the Monitoring Branch.

[3] Recoveries could be substantially higher than indicated here because OP records did not reflect the disposition of about $1.7 million in overpayments for two transactions. Although FM records indicated that about $43,000 was collected for one of the transactions, OP records did not include any documentation on the final disposition of the outstanding balance (about $73 1,000) for the transaction. Regarding the second transaction, one major news source reported that one of **USAID** CIP suppliers received the largest single combination of a fine and restitution in United **States** history for fraud for a transaction valued at nearly $1 million. However, OP did not **record** an overpayment recovery from the supplier.

[4] This amount includes about $420,000 that was reimbursed to the Department of Justice that was not included in OP records.

[5] The potential recovery was significantly reduced by $3 million because the supplier only repaid $420,000 of the $3.4 million identified as an overpayment before filing for bankruptcy protection through the U.S. court system.

[6] 1996 appears to be an aberration brought about by two large recoveries of $1.1 million in voluntary refunds resulting from OIG investigative actions. These $1.1 million included transactions that OP approved in 1992 and 1994. According to OP transaction file information, discrepancies were noted as a **result** of a commercial dispute in one case. In the second case, a supplier complaint of substandard product and an ITS **referral** to investigators prompted an investigation which resulted in the substantiation of an overpayment. However, OP did not **identify** or record the overpayments until **after** the refunds were received in the branch **office** in 1996.

From 1990 to 1997, OP's Monitoring Branch identified approximately $9.2 million in overpayments, Of the $9.2 million in overpayments identified, USAID records indicate that approximately $3.9 million, or 42 percent, was actually refunded to the U.S. government. However, because OP did not always record overpayments that yielded refunds to the government, overpayments identified and recovered may be greater than OP records indicate. Of the $5.3 million difference between the amount identified and refunded, USAID made administrative adjustments to write off about $3 million, primarily because the supplier filed for bankruptcy before the total overpayment was repaid to the government. However, for the remaining $2.3 million, neither OP nor the Office of Financial Management (FM) could provide us documentation to indicate whether a refund was paid to the government or to substantiate why the amount was not refunded. In response to our draft audit report, OP provided us with documentation that identified 7 additional uncollected overpayments from transactions processed as long ago as 1981. As a result, the total amount owed to the government is more than the $2.3 million identified in this report.

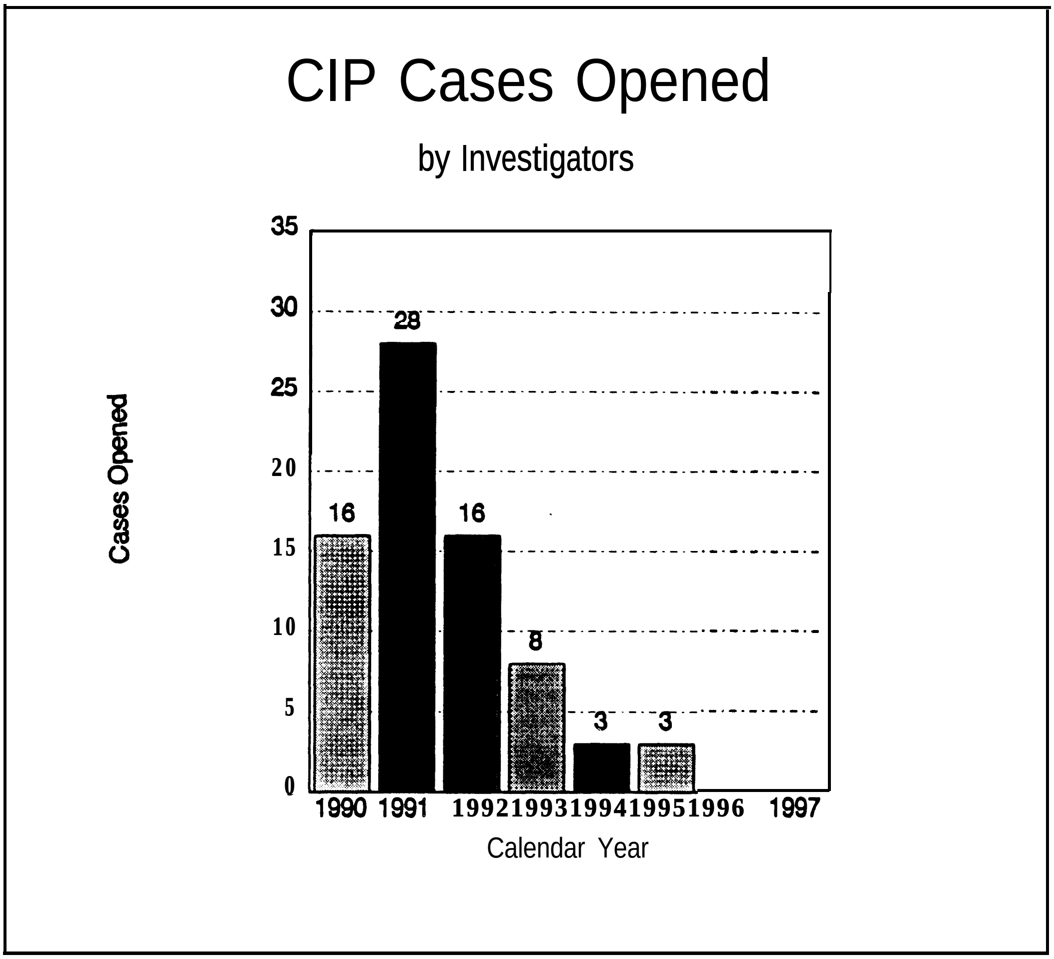
The post transaction reviews also served as a deterrent to discourage overpricing and encourage voluntary refunds when overpricing occurred. These voluntary refunds also declined when post transaction reviews stopped. Branch staff told us that because suppliers were aware that USAID might perform a post transaction review within three years after a transaction occurred, some companies that regularly conducted CIP business would submit voluntary refunds before a post transaction review was conducted. Routinely, some ITS and the Branch Chief received notification of overpayments and subsequently received suppliers' checks for overpayments. (Appendix IV provides a chart that tracks the flow of a supplier's voluntary refund check when it was received by Monitoring Branch staff).

Associated Investigations Stopped
<u>and Recoveries Plummeted</u>

In addition to the $3.9 million recovered by the Monitoring Branch, post transaction reviews led to a number of criminal investigations. The result of 13 criminal investigations by OIG/I included about $8.1 million in additional recoveries to the government from fines, disallowed costs, and transaction cancellations between 1990 and 1995. In addition, investigations resulted in criminal convictions for fraud and suspensions and debarments to prevent unscrupulous suppliers from participating in the program.

Routinely, during the course of reviewing supplier's commodity applications and proforma invoices and conducting post transaction reviews, the ITS provided major leads regarding potentially fraudulent activities to OIG/I for further examination. The ITS and investigators worked closely together to uncover fraud-related issues beyond commodity transaction pricing irregularities such as product substitution, false contractual statements, and source/origin violations. With the suspension of post transaction reviews, however, the referrals from the ITS to OIG/I declined and a major source of information about possible fraud or misuse of funds was lost.

As a result, the number of CIP cases investigated dropped from, a high of 28 cases in 1991 to zero in 1996 and 1997 and the resulting recoveries from these investigations also dropped to zero. (The following graph shows the number of CIP investigations opened by year.)



Post Transaction Review
<u>Function Was Cost Effective</u>

Our review of the CIP transactions and staffing records found that the branch's earlier review activities were very cost effective-recovering about $10 for every dollar spent conducting the reviews.

OP records show that, before OP suspended the reviews, the branch identified overpayments, on average, amounting to about $2.6 million a year from post transaction review activities. The estimated salary cost of these review activities is between $74,000 to $78,000. Thus, the branch identified about $33 in overpayments for every dollar invested. After the suspension, overpayments identified declined to an average of $302,000 per year or about $4 in overpayments for every dollar invested.

Similarly, actual recoveries significantly exceeded costs. Before the suspension of post transaction reviews, average annual recoveries were about $808,000 or about $10 for every dollar invested in the reviews. After the reviews were suspended, the recoveries dropped, on average, to about $299,000 per year, or less than $4 for every dollar invested.

OP officials told us that they believed post transaction reviews were not cost effective because refunds collected were less than monitoring branch expenses. Although OP's cost analysis was not documented, their oral assumption overstated actual costs to conduct the reviews and understated the amount of overpayments identified and recovered. Overpayments were understated, because voluntary refunds were not considered, even though many voluntary refunds were negotiated settlements of overpayments identified from monitoring branch activities. Also, OP did not consider the role played by the Monitoring Branch as (1) a stimulus for suppliers to voluntarily refund overpayments, (2) a deterrent to overpricing by some suppliers or (3) the primary source of information about fraudulent activity.

OP officials told us that they estimated the cost of performing post transaction reviews to be $300,000 to $350,000 per year. This estimate was based on the assumption that four employees worked full time doing post transaction reviews and were paid $50,000 per year or a total of $200,000. OP then added an additional 65 percent or $130,000 for employment expenses such as rent and employee benefits. However, we found that this overstated post transaction review costs.

Although OP estimated costs based on the assumption that the ITS spent 100 percent of their time conducting post transaction reviews, the branch chief and the ITS estimated that about 30 percent of the specialists' time was spent performing reviews. Further, the Budget Office told us that operating costs such as rent and equipment are considered fixed costs that should not be included in the calculations. For this reason, the 65 percent burden rate applied by OP would not be appropriate. Instead, the Budget Office stated that the method used to calculate personnel costs should take average salary costs plus employee benefits. During the six-year period from 1990 to 1995, employee benefits ranged from 13 to 25 percent, depending primarily on the employee's retirement system. The branch employed five ITS in 1990 and 1991 and four ITS between 1992 and 1995.

To evaluate the branch's cost effectiveness we computed ITS cost using actual salary plus the Budget Office's guidance for employee benefits costs. Hence, the average annual cost to perform all branch activities for the six years (1990 to 1995) was between $248,000 and $260,000, depending **on the** ITS' retirement system. Because branch staff only spent 30 percent of their time conducting post transaction reviews, the annual cost to perform post transaction reviews was between $74,000 and $78,000.

In order to ensure that USAID (1) complies with the pricing provisions of the FAA and federal regulations, and (2) provides a viable deterrent to supplier overpricing, we are recommending the following:

<u>Recommendation No. 1:</u> We recommend that the Assistant Administrator, Bureau for Management, develop a cost-effective approach to perform post transaction reviews through a systematic selection of transactions to be reviewed.

Internal Control Deficiencies <u>Increase Risk of Fraud and Abuse</u>

GAO's Standards For Internal Controls In The Federal Government require that federal agencies implement a system of internal controls to ensure assets are protected against waste, loss, unauthorized use and misappropriation. However, OP management has not implemented an effective system of internal controls over the CIP transaction review process. In this regard, OP has not established the critical elements of specific internal controls related to (1) separation of duties, (2) documentation, and (3) recording of transactions and events. Since OP did not establish these critical internal control elements, USAID does not have reasonable assurance that CIP program assets are properly safeguarded against waste, loss, and unauthorized use. Specifically, internal controls do not ensure timely determination, receipt, and deposit of supplier refunds as reflected in the fact that OP and FM officials could not account for the disposition of more than **$2.3** million in identified CIP overpayments.

An effective system of internal controls is required by the General Accounting Office (GAO) standards in order to implement the Federal Managers' Financial Integrity Act of 1982 and the Accounting and Auditing Act of **1950.** GAO developed five general and six specific internal control standards to be followed by executive agencies in establishing and maintaining systems of internal control and defined the minimum level of quality for an acceptable internal control system. The six specific standards address **(1)** documentation, (2) recording of transactions and events, (3) execution of transactions and events, **(4)** separation of duties, (5) supervision, and **(6)** access to and accountability of resources. We found deficiencies in three standards related to separation of duties, documentation, and recording of transactions and events that increase the risk of fraud, waste, and abuse.

<u>Separation of Duties</u>

GAO specific internal control standards stipulate that key duties and responsibilities in authorizing, processing, recording, and reviewing transactions should be separated among individuals to reduce the risk of error, waste, wrongful acts, or to reduce the risk that such undesirable acts may go undetected. Nonetheless, OP employed a management practice of assigning critical actions associated with a transaction to one ITS.

The ITS' combined duties of recommending the approval of the transaction, identifying overpayments, and receiving supplier refund checks, increased the risk that assets might not be safeguarded against waste, loss, unauthorized use, and misappropriation. By the scope of their duties, the ITS had to develop a close rapport with suppliers with whom they frequently interacted.

We believe that USAID could reduce this vulnerability by ensuring that specific processes (such as the receipt of overpayment checks) are not handled by the same individual who initially reviewed and recommended approval of the transaction. As a result, we are recommending the following:

Recommendation No. 2: In order to ensure that no one individual controls or appears to control all key aspects of a single transaction, we recommend that the Assistant Administrator, Bureau for Management increase management supervision regarding the separation of duties.

Documentation

GAO's specific internal control standards require that all transactions and other significant events be clearly documented and that documentation be readily available for examination. However, our review of about 3,800 transaction records from **1991** to 1995 indicated that, in most instances, the Monitoring Branch employed poor documentation and record-keeping practices. ITS did not maintain commodity transaction records in a consistent and unified manner due to a lack of guidance and procedures on documentation. The detail to which a commodity transaction file was documented was directly related to the individual specialist who maintained the file. In a 1994 audit report, the OIG recommended that USAID better document its price analyses of CIP transactions.[7] Also, in 1994, management recognized the need to improve review procedures and documentation standards. However, a new post transaction checklist was not finalized until 1995 and by that time post transaction reviews had already stopped.

Also, OP management did not ensure that adequate documentation was compiled. For example, in most transaction files, we found ITS did not record key information when an overpayment was identified. This information included such things as (1) the date that the overpayment was discovered, (2) a detailed computation of the amount owed, (3) the evidence supporting the overpayment, (4) dates of contact with the supplier requesting a voluntary refund and the outcome of negotiations, (5) a copy of the check received from the supplier, and **(6)** a copy of a Notice of Collection/Adjustment used to record an anticipated voluntary refund.

[7] Audit of USAID Policies and Procedures Over USAID/Jordan's Private Sector Commodity Import Program, Report No. 9-000-94-012, July 29, 1994.

We believe the Assistant Administrator, Bureau for Management should specify the documentation requirements for establishing voluntary refunds and records within a transaction file that will provide valuable information regarding such things as the date the overpayment was discovered, a computation of the overpayment, and the date of supplier notification and disposition. At a minimum, the Assistant Administrator, Bureau for Management should ensure that documentation is standardized to provide sufficient and consistent information regarding CIP transactions. In addition, the Assistant Administrator should ensure that the transaction documentation includes a copy of the supplier's check and other supporting documentation. Therefore, we are recommending the following:

Recommendation No. 3: We recommend that the Assistant Administrator, Bureau for Management establish documentation requirements that provide sufficient information about transactions including such things as the overpayment discovery date, a detailed computation of the overpayment, supplier contact date and disposition, check copies, and supporting financial documentation for funds owed to USAID.

Recording Transactions and Events

GAO specific internal control standards require that transactions and other significant events be promptly recorded and properly classified. Specifically, the standard applies to the entire process or life cycle of a transaction or event including the initiation and authorization, processing, and the final classification of those transactions and events in summary records.

The Monitoring Branch did not always record identified overpayments, anticipated negotiated refunds, or the disposition of identified overpayments. The Branch did maintain a handwritten log of overpayments that showed the branch's receipt of suppliers' checks resulting from voluntary refunds. However, no suspense file was created as a management tool, to record and track anticipated negotiated overpayment refunds. Although we found evidence of identified overpayments for some transactions, OP could not provide us with documentation to indicate whether some of the overpayments were received. Consequently, OP management could neither track anticipated negotiated refunds, provide an estimate of refunds that should be credited back to the program, or provide follow-up if the refunds were not received in a timely manner. For example, as discussed earlier in this report, of the more than $9.2 million in CIP overpayments, FM and OP were able to verify that only $3.9 million was recovered. OP officials administratively reduced about $3 million but could not account for the disposition of more than $2.3 million in identified overpayments. Without properly recording overpayments identified, anticipated recoveries, and other events, OP management was not knowledgeable about the number of overpayments identified, the dollar amount of the overpayments, and when to expect payment. Consequently, OP was not in the best position to issue a timely Bill For Collection if a supplier failed to remit payment as agreed.

Also, OP and FM did not establish procedures to ensure that negotiated voluntary refunds were recorded as a debt owed the U.S. government until the refund check was received. The

Debt Collection Improvement Act of 1996 specifies that a debt is any amount of funds or property that an appropriate official of the federal government has determined is owed to the United States by a person, organization, or entity- Moreover, a debt and receivable is created when a responsible federal official determines that an amount is owed. According to this definition, a voluntary recovery would be a debt if the ITS and the supplier have reached agreement that the supplier owes the U.S. government money. USAID Handbook 19, Chapter 7, AID Billing and Collection Procedures, however, does not contain specific guidelines for documenting a negotiated financial settlement. Furthermore, there is no indication that FM provided oversight/liaison activities with the Monitoring Branch as the only non-FM billing office within USAID. As a result, FM did not receive documentation from OP to record negotiated voluntary refunds as a USAID account receivable. In effect, FM did not have visibility of negotiated voluntary refunds until they actually received the check.

To ensure that transactions and events are properly recorded, we are recommending the following:

Recommendation No. 4: We recommend that the Assistant Administrator, Bureau for Management:

4.1 strengthen internal controls by specifying procedures and responsibilities for recording identified overpayments and the receipt of voluntary refunds.

4.2 identify and make a final management decision on all outstanding overpayments, including the $2.3 million noted in this report.

4.3 establish procedures to account for negotiated voluntary refunds.

OP Management Has Not Demonstrated Support For Enforcing CIP Price Provisions

GAO's Standards for Internal Controls in the Federal Government emphasize that managers must maintain and demonstrate a positive and supportive attitude toward internal controls. The fact that OP has not conducted post transaction reviews for over four years and has not implemented an effective system of internal controls indicates that OP management has not shown a supportive attitude towards enforcing the price provisions contained in the Foreign Assistance Act and federal regulations. As a result, OP has not fulfilled its responsibility to prevent overpricing and to identify and recover overpayments. Further, OP management has not adequately supported its rationale for suspending post transaction reviews. Although OP management has initiated efforts to replace post transaction reviews with a preshipment review program, after three years, OP has not implemented the preshipment reviews. In addition, OP has not analyzed the costs and benefits of preshipment reviews. Both

USAID/Cairo and the Government of Egypt (GOE) oppose replacing post transaction reviews with preshipment reviews.

Management Reasons For Suspending Post Transaction Reviews

Since 1995, OP management has provided several reasons for suspending post transaction reviews. In April 1995, the OIG initiated an investigation based on an allegation that OP had stopped conducting post transaction reviews. Responding. to the OIG investigator's questions, the OP Director sent a June 1995 memorandum to the OIG/I stating that OP had temporarily suspended the distribution of post transaction reviews in order to clear a backlog of uncompleted cases and to revise the review procedures. The memorandum stated that the reviews had resumed one month earlier, in May 1995. Based on OP assurance that post transaction reviews had resumed, the OIG investigation was terminated. However, during our current audit, we found that OP Monitoring Branch (1) performed only 4 post transaction reviews in 1995, (2) did not clear its backlog of uncompleted cases, and (3) did not use the new procedures. According to ITS and OP managers, at the time the investigators were looking into the suspension, OP managers distributed about 25 CIP transaction files to each ITS for post transaction reviews. However, very few of the cases were actually completed.

In July 1996, OIG/I again questioned OP officials about the suspension of post transaction reviews. At that time, OP officials stated that they had stopped the post transaction reviews in order to shift to preshipment reviews, which would begin after a reduction-in-force (RIF) was completed. A preshipment review is designed as a cursory review to ensure compliance with price and other eligibility requirements before the commodity is shipped, rather than after the transaction is completed. As USAID's agent, a contractor would review commodity contract documents for a limited number of transactions to confirm that the commodity meets the importer's requirements and verify that the commodity meets USAID source, origin, and price requirements. In addition, a physical inspection of the commodities may be conducted prior to shipment. In this regard, the officials stated they planned to contract with a private sector firm to perform the preshipment reviews. Although the RIF was completed in late 1996, OP had not started the preshipment review program when we began this audit in July 1997.

When we began the current audit, OP officials told us that (1) they stopped performing post transaction reviews because they were not cost effective, and (2) they still planned to implement a preshipment review program. However, as pointed out earlier in this report, post transaction review activities were actually very cost effective. In addition, when we completed this report in September 1998, OP still had not implemented the preshipment review program.

Preshipment Review Program Not
Supported by Adequate Analysis

OP's plan to implement a preshipment review program has also not been supported by adequate analysis of costs and benefits. Significant program changes, such as initiating a preshipment review program, should be, but were not supported by a cost benefit analysis. As a result, OP management has not determined what benefits will be achieved from conducting preshipment reviews, the costs to perform inherently governmental functions,* or the cost to conduct a preshipment review. Regarding review costs, OP officials told us they plan to limit contract costs to $200,000, which they believe will allow the contractor to review from **7** to **20** percent of CR? transactions. Without cost and benefit information, OP does not have an adequate basis to compare the costs and benefits of preshipment reviews to post transaction reviews. In fact, preshipment reviews may not ensure that final prices do not exceed the prevailing market price in the U.S., as adjusted. Because the reviews occur prior to shipping, cost estimates may not reflect final costs. When we discussed this limitation with OP officials, they agreed that preshipment reviews might not fully substitute for post transaction reviews and planned to retain the authority to conduct post transaction reviews on an as needed basis.

Preshipment Review Not
Supported by USAID/Cairo
and Government of Egypt

USAID/Cairo officials oppose the effort to substitute preshipment reviews for post transaction reviews. These officials told us that OP had not provided an analysis or justification demonstrating that preshipment reviews would provide significant benefits compared to post transaction reviews. Mission management continues to support the use of post transaction reviews to ensure compliance with the price provisions of the FAA. USAID/Cairo also believes the preshipment review program should be rejected because it would place USAID in the middle of a private commercial transaction, which could substantially increase the USAID's liability in the event of disputes. Based on experience with lawsuits in Egyptian courts, USAID/Cairo officials believe that Egyptian courts could interpret USAID's right to conduct preshipment reviews as an obligation to do so. Because many transactions will not have been reviewed, under this interpretation of Egyptian law, if an importer incurs damages, USAID could be considered a guarantor even if it had not performed a review.

Furthermore, the GOE objects to a preshipment review program and has stated to USAID/Cairo officials that they will request a waiver from the requirement if it is put into effect. In addition, the GOE opposes funding preshipment reviews with CIP program funds. Although the Egyptian CIP is the largest active CIP that USAID administers, OP officials told

* An inherently governmental function is, by nature, a function that must be performed by the government and can not be delegated to a private sector entity. An example of an inherently governmental function in the CIP is the initial approval of a transaction.

us that they would probably grant a waiver to USAID/Cairo to exempt it from any preshipment review requirement. If that were the case, few if any preshipment reviews would take place, raising further questions about the value of preshipment reviews.

In responding to a draft of this report, management's comments were generally unresponsive to the recommendations, and in fact, the comments indicate a continuing lack of a supportive attitude towards enforcing the price provisions of the Foreign Assistance Act and establishing an effective system of internal controls. Because we believe a supportive attitude is key to program success and to protecting assets from fraud, waste, and abuse, we make the following recommendation with the intent of highlighting the need to improve OP's attitude towards enforcing pricing requirements and establishing effective internal controls.

<u>Recommendation No. 5</u> We recommend that the AA/M raise the continuing lack of a supportive attitude on the part of OP management as a potentially reportable control deficiency at the next quarterly Management Control Review Committee meeting.

Conclusions

OP management has not met its responsibility to ensure compliance with legislative requirements to prevent overpricing or regulatory requirements to conduct post transaction reviews. Without these reviews, USAID's ability to identify and recover overpayments has been substantially hindered. Furthermore, USAID has not had assurance that commodities are eligible, suitable, and appropriate.

OP management's lack of a supportive attitude toward the CIP and its management controls raises questions about management's efforts to ensure that government assets are safeguarded against waste, loss, unauthorized use, and misappropriation. Good internal controls in the government are essential to good management. Management has the ultimate responsibility to develop and implement good internal controls in order to facilitate the achievement of management objectives and to serve as checks and balances against undesired actions. In this case, USAID management needs to ensure that OP meets its internal control responsibilities.

USAID needs to ensure compliance with legislative and regulatory requirements concerning post transaction reviews of the CIP, improve controls over the CIP transaction review process, and reassess its decision to implement the Preshipment Review Program.

SCOPE AND METHODOLOGY

Scope

We conducted this audit because of an allegation received by the Office of Inspector General regarding the Office of Procurement's (OP) suspension of post transaction reviews of Commodity Import Program (CIP) transactions in 1993. Our audit was designed to determine if USAID conducted post transaction reviews and other reviews of the CIP in accordance with applicable laws and regulations. We reviewed all 3,800 transactions processed from 1991 to 1995.

We conducted this audit between September 1997 and September 1998 in accordance with generally accepted government auditing standards. However, we are not able to fully answer the audit objective because OP management would not provide us with a written confirmation that, to the best of their knowledge and belief: (1) all essential information was provided to us, (2) the information provided was accurate and complete, and (3) management had followed USAID policies. Without these confirmations from OP management, we cannot fully determine if OP did what it is required to do. While we cannot state positively that OP management followed its policies and regulations, this lack of a management confirmation did not preclude us from reporting on problem areas that came to our attention.

Methodology

During our audit, we interviewed cognizant managers and staff from the Offices of Procurement, Financial Management, Inspector General, General Counsel, and USAID/Cairo regarding OP's post transaction review policies, procedures, and federal regulations. To understand established policies, procedures, and federal regulations for the CIP program, including requirements to conduct post transaction reviews, we reviewed the Foreign Assistance Act of 1968, USAID Regulation 1, USAID Handbook 19, the Debt Collection Act of 1996, and GAO's Standards for Internal Controls In The Federal Government. In addition, we reviewed OP's draft revisions and final revision to USAID Regulation 1 to include a Preshipment Review Program Plan, as well as the proposed statement of work for the Preshipment Review Program.

We determined the number of CIP post transaction reviews conducted and the review findings from available Monitoring Branch transaction files. In addition, we examined internal controls as they related to the CD? processes for approving transactions, conducting post transaction reviews, and obtaining refunds of supplier overpayments. We tested internal controls to assess the extent to which the branch's processes were vulnerable to fraud, waste, or abuse.

To determine the number of CIP transactions that the branch approved in a five-year period from 199 1 to 1995, we reviewed 3,800 readily-available Washington branch files. Also, we determined the number of post transaction reviews the branch conducted during this timeframe, and identified the transaction approval date, receiving country, supplier, commodity costs, financing method, and OP reviewer. Moreover, we were able to determine the number of post transaction reviews conducted and subsequent price adjustments from the records that OP provided to us for review.

Furthermore, to determine the number of overpayments the branch identified and the funds recovered, we obtained information from the Monitoring Branch Refunds Log and USAID/Cairo's Commodity Management Division Office's Refund Log. We then compiled proforma data sheets using these two sources of information to prepare a preliminary list of overpayments identified and recovered. We compared our preliminary list to OIG Investigator case results data and added additional information regarding suppliers who were not included in the branch and mission data. We used data from these three offices to compile a final master list of overpayments identified and recovered that we reconciled FM's CIP transaction records to determine the actual CIP recoveries made.

To evaluate the branch's cost effectiveness, we calculated total average costs for salaries for six years from 1990 to 1995 using guidance from the Budget office to estimate costs. First, we assumed that all of the International Trade Specialists (ITS) were Federal Employees Retirement System (FERS) employees, using the higher total costs for salaries and benefits.

We calculated the total salary and benefit costs for the most (5) ITS employed during this timeframe and multiplied the result by 30 percent, the amount of time estimated to complete the post transaction review function. Second, we averaged the identified overpayments from 1990 to 1992, before the post transaction reviews were suspended and divided the result by the average cost of salaries and benefits for the ITS as FERS' employees. Furthermore, using the average for identified overpayments for 1990 to 1992, we used the same method to calculate the branch's costs using OP's estimated branch costs. To assess internal controls, we reviewed the Monitoring Branch's documentation for approving, processing, and reviewing transactions. We also reviewed both OP and Office of Financial Management (FM) policies and procedures for establishing, documenting, and executing Bills For Collection and voluntary refunds for monies owed to the government. Also, we interviewed OP and FM officials.

We also reviewed the plan to begin a Preshipment Review Program as an alternative to conducting post transaction reviews, as well as the draft revisions to USAID Regulation 1, and the proposed drafts of the statements of work for the Preshipment Review Program.

To the extent possible, we assessed the proposed regulation changes to include a Preshipment Review Program to ensure suppliers' compliance with federal regulations. We also reviewed several draft proposed rule changes to USAID Regulation 1 and subsequent changes to the draft rule, two proposed statements of work, representative contractor commercial preshipment guidelines, and correspondence between Cairo mission and USAID Bureau and OP officials.

U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

SEP 16 1998

MEMORANDUM

TO: IG/AIG/A, Everette B. Orr

FROM: AA/M, Terrence J. Brown

SUBJECT: Audit of Post Transaction Review Activities Under the Commodity Import Program (Draft Audit Report No. A-000-98-m-P)

This memorandum provides Agency comments on the audit findings and recommendations in the draft report on the post transaction reviews under the Commodity Import Program (CIP).

The audit concluded that the Office of Procurement (M/OP) suspended post-transaction reviews in 1993 and that USAID has not ensured that commodity transactions met the pricing requirements of the Foreign Assistance Act.

OIG Analysis:

This comment does not accurately describe our conclusion, which is:

"OP management has not met its responsibility to ensure compliance with legislative requirements to prevent overpricing or regulatory requirements to conduct post transaction reviews. Without these reviews, USAID's ability to identify and recover overpayments has been substantially hindered. Furthermore, USAID has not had assurance that commodities are eligible, suitable, and appropriate.

OP management's lack of a supportive attitude toward the CIP and its management controls raises questions about management's efforts to ensure that government assets are safeguarded against waste, loss, unauthorized use, and misappropriation..."

The transaction reviews were not discontinued in FY 1993, but rather the assignment of new cases was suspended pending the reduction of a large backlog and the preparation of new review procedures. Based on expert knowledge, a minimum of 200 post-transaction reviews were completed during 1995 and 1996. The reviews were suspended in September 1996 due to staff reductions resulting from the Agency-wide reduction-in-force.

OIG Analysis:

This comment is not responsive to our report. Our draft report did not state that post transaction reviews were discontinued in 1993. Instead, as described in USAID's comment, the draft report stated that OP management told us that OP suspended the reviews to reduce a backlog of cases and revise the review procedures, However, our report also stated that OP had not reduced the backlog, and that the revised procedures were not used because OP had stopped conducting post transaction reviews.

USAID's assertion that a minimum of 200 cases were completed during 1995 and 1996 is not accurate or responsive to the problems identified in our report. In fact it appears to continue a pattern of misleading or inaccurate statements. OP management was unable to provide evidence that 200 reviews had been-completed. Instead, the responsible official stated that she recalled distributing about 200 cases during that period of time. In contrast, our report was based on a review of all transactions completed between 1991 and 1995, which identified four reviews completed in 1995 and 13 reviews completed in 1996. Throughout our audit OP management told us that they believed no reviews were conducted in 1996.

More disturbing than the misrepresentation of the number of reviews completed is that our draft report pointed out that OP distributed these cases in 1995, at the time that OIG/I was investigating allegations that OP had stopped conducting reviews. OIG/I terminated the investigation based on OP's assurance that the reviews had resumed (supported by the fact that cases had been distributed). Our report points out that although the cases had been distributed, few were actually completed. We believe management's comment would have been more productive had it explained why OP distributed the cases, but did not ensure that the cases were completed.

We have continued to take steps to identify over-pricing in commodity transactions. From 1993 to date, OP has reviewed in excess of 4,000 Forms AID-11, "Application for Approval of Commodity Eligibility/ In this form, U.S. suppliers are required to provide information about the commodities they intend to ship to Egyptian CIP participants. This information includes a description of the commodities, their relevant U.S. Department of Commerce schedule B numbers, information about the source and origin of the commodities and their components, identity of the producer, and the FOB/FAS cost of the commodities. Prices that appear to exceed industry norms are examined at the Form AID-II stage. Changes can be required in these transactions because of overpricing just as they can be, and sometimes are, due to ineligibility of the commodity, its components, or its place/country of production.

OIG Analysis:

This comment is also not responsive to the problems identified in our draft report. Our report describes the Form 11 review process and notes its purpose. Our report also points out that the Form 11 review is not a substitutes for post transaction reviews because it occurs before all actual prices are established.

Moreover, the private sector CIP is less vulnerable to pricing violations than its predecessor public sector program, Private sector importers repay in local currency all costs associated with these transactions. They are competitive businesspersons who use our program to increase the effectiveness of their businesses in the local marketplace. This is a significant price control in a private sector CIP.

OIG Analysis:

This comment is misleading. Although the private sector program may be less vulnerable to abuse, abuse still occurs. In fact, our analysis shows that virtually all the recovered overpayments ITS identified were private sector transactions.

We have negotiated the transfer of the post-transaction review function to USAID/Cairo since that mission has the Agency's only remaining CIP program. USAID/Cairo has accepted the function and transitional training has been approved and scheduled for September. The agreed upon transfer date is January 1, 1999.

Our response to the audit recommendations is provided below. Comments on specific sections of the report are provided in Attachment A.

<u>Recommendation No. 1:</u> We recommend that the Assistant Administrator, Bureau for Management, require OP to develop a cost-effective approach to perform post transaction reviews through a systematic selection of CIP transactions to be reviewed.

As noted above, the post-transaction review function will be transferred to USAID/Cairo effective January 1. USAID/Cairo has already concluded that the most cost effective approach is to contract out the program. Given the planned course of action, this recommendation is not applicable.

OIG Analysis:

As part of our analysis of these comments, we obtained documentation describing the planned transfer of responsibilities to USAID/Cairo. OP provided a recent exchange of letters between the AA/M and the USAID/Cairo Mission Director. Although these letters describe the transfer of some functions to USAID/Cairo, including the post transaction review function, they do not include clearly assigned roles and responsibilities. In addition, we have not been provided any analysis showing that USAID has (1) determined this to be the most cost effective approach to conducting the reviews or (2) developed a systematic process to select the transactions to be reviewed. As a result, we do not agree that this response represents a management decision to implement recommendation 1 However, we have revised the recommendation to eliminate the reference to OP performing the function in order to provide management more flexibility to implement the right solution.

Recommendation No. 2: **We recommend that the Assistant Administrator, Bureau for Management, require OP to increase management supervision regarding the, separation of duties within the branch in order to ensure that no one individual controls or appears to control all key aspects of a single transaction; such as responding to inquiries, approving a transaction, conducting a post transaction review, negotiating a financial settlement, and receiving a refund.**

The recommendation is not applicable. The transitional training for USAID/Cairo will include the importance of separation of duties and other controls in carrying out this function. Since USAID/Cairo has already decided to contract out the function, it is unlikely that separation of duties will be a significant issue.

OIG Analysis:

This comment is not responsive to the recommendation and, in our opinion demonstrates a continuing lack of a supportive management attitude towards effective internal controls. First, training is not a substitute for a properly designed and instituted system of internal controls. Second, contracting out is also not an automatic solution to the problem. To ensure that controls reduce the existing vulnerability to waste, loss, unauthorized use and misappropriation of USAID funds, and effective system of internal controls that incorporates separation of duties is needed. We do not agree that this response represents a management decision to implement recommendation 2.

Recommendation No. 3: We recommend that the Assistant Administrator, Bureau for Management, require OP to establish documentation requirements that provide sufficient information about CIP transactions including such things as the overpayment discovery date, a detailed computation of the overpayment, supplier contact date and disposition check copies, and supporting financial documentation for funds owed to USAID.

The recommendation is not applicable. We will also stress the importance of adequate documentation in the training. As the auditors no doubt noticed from the on-site visit conducted during this audit, the commodity staff in USAID/Cairo has an excellent transaction tracking system and very thorough files on program participants (importers). I have every confidence that these new functions will be carried out with the same proficiency and regard for detail and documentation as are the current mission CIP activities.

OIG Analysis:

This comment is also not responsive to the recommendation and, in our opinion demonstrates a continuing lack of a supportive management attitude towards effective internal controls. Again, training- **is not** a substitute for an effective system of controls, If USAID/Cairo does take on new CIP functions, documentation requirements will need to be defined. We do not agree that this response represents a management decision to implement recommendation 3.

Recommendation No. 4: We recommend that the Assistant Administrator, Bureau for Management require OP to:

4.1 **strengthen internal controls by specifying procedures and responsibilities for recording identified overpayments and the receipt of** voluntary refunds **from** CIP.

4.2 **determine the final disposition of** $2.4 **million in identified overpayments for which** no **documentation exists.**

4.3 **ensure that the Office of Financial Management and the Office of Procurement establish procedures for the Office of Procurement's role (as a non-Office of Financial Management billing office) in the collection of refunds from suppliers.**

M/OP and M/FM have agreed that the Monitoring branch (now the Commodity Branch) in OP should no longer act as a billing office. Further, effective **February 1998, M/FM transferred responsibility for issuance** and maintenance of all of the direct bank letters of commitment that support the CIP in Egypt to the

Financial Management Office of USAID/Cairo. In the transitional training, we will emphasize the importance of adequate procedures for recording overpayments and the receipt of voluntary refunds. Recommendations 4.1 and 4.3 are also not applicable.

With regard to recommendation 4.2, the final disposition of $2.4 million has been determined to the extent that documentation exists. Identified overpayments will not always equal recovered overpayments for a variety of legitimate factors. A bill for collection can be issued for an amount that appears to the analyst to be an appropriate refund. Subsequent correspondence often leads to the downward revision of a bill and the collection of a lesser, but entirely appropriate amount. Available documentation indicates that $1.3 million has been written off or is in the process of write-off. We are unable to locate the documentation for the remainder of the administrative adjustment.

OIG Analysis.:

USAID's decision to emphasize training to ensure that identified overpayments and negotiated voluntary refunds are properly recorded is not responsive to our recommendation. We do not agree that this response represents a management decision to implement recommendation 4.1.

The explanation of the factors that reduce the amount collected from the amount identified was already described in our draft report. When we asked for support that USAID had or was in the process of writing-off $1.3 million, we were provided a draft letter from OP to FM requesting that 10 cases, going back as far as 1981 be written off as uncollectible. About $1.1 million of that amount related to cases we identified, leaving $1.2 million still unaccounted for. Further, the fact that USAID identified outstanding overpayments in addition to the cases covered by our audit shows that additional uncollected overpayments also exist. These too should be subject to a final management decision. We do not agree that this response represents a management decision to implement recommendation 4.2. We did revise the recommendation to recognize that other outstanding overpayments not identified in our review should be included.

USAID's decision that OP will no longer act as a billing office is responsive to our recommendation 4.3. We agree that this response represents a management decision to implement recommendation 4.3.

Finally, you indicated that the auditors were not assured that all relevant information was provided during the course of the audit. The M/OP staff has assured me that they provided all available information to the audit team, including 19 boxes retrieved from Agency archives.

Thank you for the opportunity to comment on the draft report. As related above, we will share areas of concern identified by the audit with USAID/Cairo as they prepare to implement the review function. While I do not anticipate any problems, your consideration of a follow-up review in Cairo following their implementation of the program is welcomed.

Attachment: as stated

Attachment A

Agency Comments:

Bottom of page 3 of the draft audit report. The Statement that “a voluntary refund is a negotiated settlement of an overpayment” is incorrect. While a voluntary refund can be the result of a negotiated settlement of an overpayment, the vast majority of voluntary refunds are entirely voluntary, i.e., they are refunded by conscientious suppliers as a matter of course and in no way can be anticipate, calculated, notated or tracked by OP staff prior to receipt. OP cannot maintain records of the unknown.

OIG Analysis:

We do not expect OP to maintain records of the unknown. However the Agency comments do not address the substantial number of instances disclosed by our audit where OP indeed had identified anticipated voluntary reimbursements for overpayments, but was not knowledgeable about the number of overpayments identified, the dollar amount of the overpayments, and when to expect payment, nor had they notified FM of the related account receivable.

While we realize that there were a few conscientious suppliers who may have submitted refund checks voluntarily before a review was conducted, our audit showed that the majority of the voluntary refunds were negotiated by International Trade Specialists. In fact, the common practice for ITS was to try to resolve any overpayment issue telephonically as a “voluntary” refund, which was less time-consuming and required less formal documentation. Under these circumstances OP had sufficient information to record and track the status of the anticipated “voluntary” refund and related receivable, although our audit showed that this was not the practice.

Agency Comments:

Page 4 of the draft audit report. Table I is incorrect. During the file review we advised audit team members that post transaction reviews were conducted at random and that the date of the transaction should not be confused with the date of the review. Since we completed about 200 reviews, we suspect that the data in the table were based on the date of the transaction.

OIG Analysis:

Table I is correct as presented in the draft report,, The table reflects the dates that post transaction reviews were completed. As noted in our report, the Monitoring Branch discontinued conducting post transaction reviews on a regular basis some time in 1993

and the OP Director also told us that he made a conscious decision to suspend post transaction reviews in 1994. While we recognize that OP management has provided several reasons for suspending regularly scheduled reviews, our audit disclosed, as shown in Table I, that the number of post transaction reviews conducted declined dramatically beginning in 1993 to a point where only 17 reviews were conducted in 1995 and 1996 (for transactions that occurred from 1991 - 1995).

After receiving the AA/M's comments stating that "based on expert knowledge, a minimum of 200 post transaction reviews were completed in 1995 and 1996" we contacted OP to determine whether there were post transaction review files for 1995 and 1996 that we had not reviewed during the audit. We were informed by the Monitoring Branch Chief that she recalled assigning about 200 post transaction reviews during the period, but that they were unable to locate the log book for assignments of post transaction reviews to ITS personnel. Regardless of whether the assignments were made, our audit disclosed that the post transaction review checklist upon which review results were recorded indicates that only four such reviews were completed in 1995 and 13 in 1996.

Agency Comments:

Page 5 of the draft audit report. Table II, OVERPAYMENTS IDENTIFIED AND RECOVERED, provides data that is misleading. Overpayments identified cannot be compared on face value to overpayments recovered. A bill for collection can be issued for an amount that appears to the analyst to be an appropriate refund. Subsequent correspondence, which the supplier is entitled to engage in if he contests the bill, often leads to the downward revision of a bill and subsequent collection of a lesser but entirely appropriate amount. Follow-on actions can further impact on collections against bills issued, e.g. settlement, bankruptcy or receivership agreements wherein the Agency accepts a lesser refund. For example, a bill was issued to a supplier in 1991 in the amount of $969,323.28. Over the course of a year the bill was revised downward several times. A total amount of $196,415.54 was collected through direct payments from the supplier and administrative offsets taken by USAID/Cairo. The supplier appealed to the Agency's GC to have the late payment and penalty interest reduced and the GC refunded $70,596.81 to the supplier. Hence, $125,818.73 was collected against the original $969,323.28, but the balance is not to be construed as uncollected or as an overpayment that lacks final disposition. In another case, the Agency accepted a settlement agreement from a bankrupt supplier for about 20 cents on the dollar on a bill issued for over $4 million. That settlement was negotiated by GC/LE, the balance of which, again, should not be viewed as an overpayment that lacks final disposition.

OIG Analysis:

The intent of the chart is not to compare on face value overpayments identified to overpayments recovered. Rather the intended purpose of the chart, when taken in context with related footnotes and text, is to correlate, and in fact it does so very well, the drastic reduction (some 61 percent) in identification and recovery of overpayments in the years immediately after OP stopped conducting post transaction reviews on a regular basis.

We agree with the Agency's comments that one cannot compare on face value overpayments identified to overpayments recovered. We recognize that any number of events can come into play that could change the final recovery amount. For example, as pointed out in the chart's footnotes, one supplier only repaid $420,000 of the $3.4 million identified as an overpayment before filing for bankruptcy protection. On the other hand, as indicated in the narrative accompanying the chart, overpayments identified and recovered may be greater than OP records indicate since there was about $2.3 million in overpayments identified for which neither OP nor FM could provide us documentation to indicate whether a refund was paid to the government or to substantiate the reason as to why the amount was not refunded.

Agency Comments:

Pages 7-9 of the draft audit report. The draft audit report uses a cost effectiveness analysis that includes large voluntary refunds that did not result from post audits. Such an analysis is inappropriate. Reorganization and reinvention of our USAID/Washington commodity branches and their functions had been determined and were underway before the outset of this audit. M/OP management had looked at the base branch recoveries associated with post audits (excluding voluntary refunds), determined that they fell below the cost of maintaining the branch at previous levels, and proposed alternative, smarter processes that would require fewer M/OP staff.

OIG Analysis:

We believe that OP management has minimized the contribution post transaction reviews made in generating voluntary refunds. Table II shows that when post transaction reviews stopped, voluntary refunds, with one exception, also declined significantly. Also, as stated in our report, post transaction reviews, in part, served as a deterrent to discourage overpricing and encourage voluntary refunds when overpricing occurred. During our audit, branch staff told us that routinely some suppliers notified OP of overpayments and forwarded refund checks to the branch before a spot transaction review was conducted. In addition, in many cases, voluntary refunds reflect the result of a post transactio review. Often, when the ITS notified the supplier that the review had identified overpayments, the supplier agreed to pay and the agreement was recorded as a voluntary refund.

Agency Comments:

Page 10 of the draft audit report. The statement that "OP employed a management practice of assigning all actions associated with a transaction to one ITS" is incorrect. USAID-financed CIP transactions are approved in Egypt by the participating Egyptian banks and USAID Mission staff. Payment instruments are advised by U.S. banks. Form AID-l 1 review by OP staff is not approval of the transaction but the first step in the review process, and is designed to find problems with the commodities to be shipped, and with the transaction in general prior to shipment so as to avoid the need for seeking refunds after the supplier has been paid. The perception that a single Branch analyst approves the transaction, identifies overpayments, receives supplier refund checks, responds to inquiries etc., is inaccurate, ignores the role of the branch supervisor, and supposes an autonomy of action that is unlikely in a small, intimate unit of seven persons. Approval of the Form **AID-1 1** approves the commodity not the transaction. All forms are approved by the supervisor after review by a branch analyst. All voluntary refunds are processed by a single branch analyst regardless of which analyst reviewed the relevant Form AID-1 1, and, like Forms AID-1 1, all submissions of voluntary refunds are reviewed and signed by the supervisor. Bills for Collection, when issued, must be cleared by the General Counsel's office. This is to ensure not only that the Bill is legally justified, but also that payment of the Bill does not end the Government's rights in a case prematurely. Lastly, all branch analysts respond to incoming inquiries, pulling appropriate files as necessary and irrespective of whether they reviewed the transaction.

OIG Analysis:

According to the evidence we obtained, it has been OP's management practice to assign critical actions associated with a specific transaction to one ITS, in most instances. These critical actions, as stated in our report, included combined duties of recommending the approval of the transaction, identifying and negotiating overpayments, as well as receiving supplier refund checks. This OP management practice exposed the Agency to vulnerabilities of undesirable acts such as error, waste, fraud, and abuse. In addition, we do not take issue that some supervisory review occurred at different stages of the life cycle of a transaction, however, in many instances supervisory review was not indicated.

Agency Comments:

Page 14 of the draft audit report. The description of preshipment review (footnote **8)** might erroneously lead one to understand that preshipment inspection companies normally undertake and are experienced at detailed price reviews. The price reviews normally accomplished by inspection firms are cursory in nature. Detailed price examinations as required by USAID Regulation **1** entail application of USAID price rules, review of commissions and other payment, determination of use of eligible delivery services, and other elements of contract performance. Inspection firms are" not normally involved in this detail. Suggest the footnote be changed to read: "OP had designed a preshipment review requirement that would seek to ensure compliance with ...."

OIG Analysis:

For more clarity, we have incorporated footnote 8 to the body of the paragraph in our report that describes preshipment review.

Agency Comments:

<u>Page 15 of the draft audit report.</u> The sentence beginning in the middle of the eighth line ("Based on a dialogue with Egyptian government officials, USAID/Cairo officials ...") should be changed to read, "Based on experience with lawsuits in Egyptian courts, USAID/Cairo officials ...."

OIG Analysis:

We have incorporated this change in the final draft of the report.

ITS DUTIES AND CIP TRANSACTIONS PROCESS

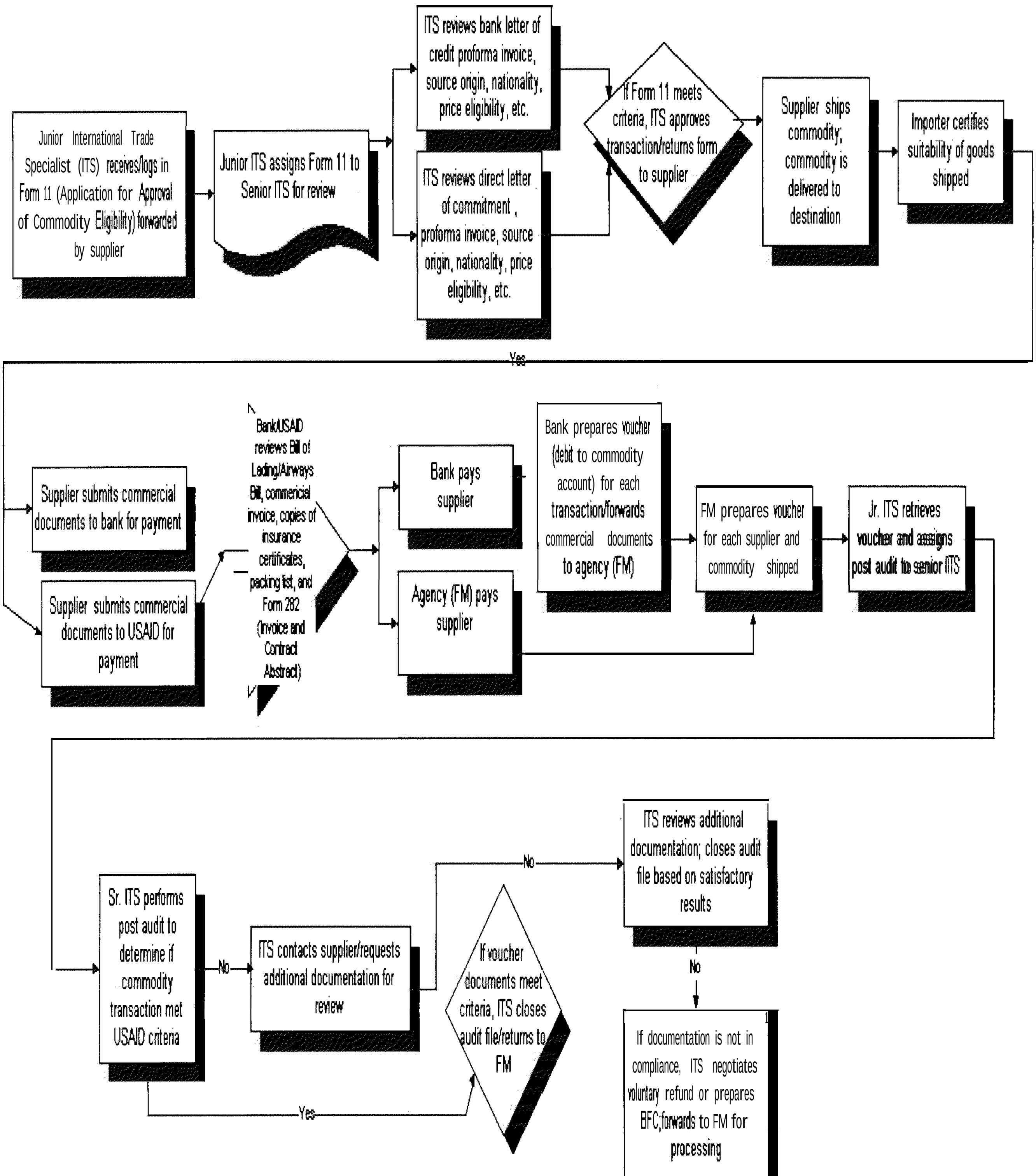
ITS Duties

Prior to performing these post transaction reviews, ITS performed various commodity review functions. For example, the ITS examined a prospective CIP supplier's commodity approval application (AID Form 1 1), a proforma invoice, and an approved bank letter of credit. In particular, during the initial review, the ITS reviewed the documents to determine the supplier's eligibility to participate in the program, the commodity's eligibility for financing, the validity of the supplier contract with the importer, and the overall commodity price estimates, After a commodity had been shipped, the U.S. supplier certified various commodity cost information by completing Form AID 282, Invoice and Contract Abstract, as a certification of commodity transaction costs. The supplier presented the Form 282 and other supporting documentation to a participating U.S. bank for payment. After reviewing the supplier's documentation, the U.S. bank paid the supplier for the goods shipped. The U.S. bank forwarded all vouchers[9] to Unsaid FM for further review. OP Monitoring Branch staff retrieved the vouchers from FM to conduct the post transaction reviews.

The detailed steps in the CIP transaction process are shown in the following chart.

[9] Transaction documentation or a voucher contains copies of the previously approved USAID Form 11, proforma invoice, bank letter of credit, Bill of Lading, freight information, insurance certificates, commissions, etc.

USAID-Washington Commodity Import Program Transactions Review Process



Voluntary Refund Collection Process